TWENTY AREAS OF CORPORATE LAW REFORM WHICH NEED TO BE ADDRESSED

SUBMISSION ON CLERP 9 PROPOSALS BY SHAREHOLDER ACTIVIST STEPHEN MAYNE

Stephen Mayne is Australia's best known shareholder activist who has failed on 18 occasions to be elected to major public company boards. Stephen spent 10 years as a business journalist working for a range of papers including The Herald Sun, The Age, The Daily Telegraph and The Australian Financial Review. In February 2000 he founded www.crikey.com.au which has become Australia's best known independent ezine with 4800 paying subscribers and 600,000 page views a month.

What follows are 20 areas of corporate governance reform that Stephen feels need to be addressed through the CLERP process after attending more than 200 AGMs and following the Australian corporate sector closely for 15 years.

1. Church and state separation between banks and fund managers

The most urgent structural issue in Australian financial services is big bank dominance of the funds management industry and the common directors between the fund managers and the stocks they invest in. The directors of our Big Four banks sit on the majority of Australia's top 50 companies and the prevailing culture is to rarely vote against a member of the directors' club.

For instance, Colonial was the largest Australian BHP shareholder but found it difficult to vote against the controversial Billiton merger in 2001 when one of the BHP directors strongly advocating the deal was CBA chairman John Ralph.

Now that banks collectively have a majority of the funds management industry how will they manage the conflicts when they have a direct debt exposure to a collapsing company and manage third party equity investments in the same company? The present Bell Resources battle in the WA Supreme Court is about precisely this point. Shareholders are alleging the banks queue-jumped in their claims over certain assets and this sort of dispute demonstrates how untenable it is to have the same organisations providing the major debt and equity flows into the economy.

The forthcoming NAB EGM will demonstrate these conflicts as many fund managers will slavishly support the incumbent directors and oppose Cathy Walter to protect the large fees NAB pays them through MLC.

2. The 100 shareholder rule, AGMs and EGMs

The requirement to get 100 signatures from shareholders to get a resolution on the notice paper at an annual general meeting is too difficult. In America you only need $US2000 worth of shares. For example, the Exxon-Mobil AGM in Dallas last May had 12 shareholder resolutions. Before this year's Boral AGM, we hadn't had 12 shareholder resolutions over the past 15 years in Australia.

In other words, public company boards have for too long had an effective monopoly over the resolutions up for debate at AGMs. If we want a culture of shareholder pressure in Australia we need to make it easier for shareholders to put resolutions to the vote.

Whilst 100 signatures is too onerous for AGM shareholder resolutions, 100 shareholders is too easy for the calling of an extraordinary general meeting which should only be a last resort option because of the additional cost it imposes on the company.

Crikey would support changes that required 5 per cent of the capital for an EGM provided it was made easier to get resolutions up at AGMs.

3. Chairmen and CEOs are accountable but directors are not

An analysis of troubled Australia listed companies over the past 15 years reveals that chairmen and CEOs are generally held accountable for problems and tend to resign in quick succession. This theory holds true with troubled companies such as NAB, AMP, Westpac, ANZ, BHP, Aristocrat, David Jones, Orica, Lend Lease, PMP and Southcorp.

Whilst this is clearly accountability at work, there is little sign that the gene pool of the director's club is deepening as the accountability does not extend to non-executive directors. For instance, former Tubemakers CEO Tony Daniels had a board portfolio that included the trifecta of duds in Pasminco, Orica and Pacific Dunlop yet he continues to be re-elected to the AGL and Commonwealth Bank boards with 99 per cent of the vote. This poor performer remains a prominent member of the directors' club and was even chairman of the $20 billion-plus NSW state super schemes a few years ago influencing how they voted on other poorly performing directors.

Similarly, how can Margaret Jackson chair the Pacific Dunlop and BHP audit committees as billions were lost in the late 1990s and then be promoted to chair Qantas? The same applies to Rick Allert at Coles Myer after the Southcorp fiasco and Graham Kraehe at NAB given his presence on the risk and audit committee and additional baggage from Brambles.

4. Broadening the directors' gene pool

The ASX Corporate Governance guidelines recommended last year that no individual chair more than one top 100 listed company but we still have seven individuals doing this. They are:

Rick Allert (Axa and Coles Myer), Don Argus (BHP-Billiton and Brambles), Charles Goode (ANZ and Woodside), Mark Johnson (Macquarie Infrastructure Group and AGL), Graham Kraehe (NAB and Bluescope Steel), James Strong (Woolworths and Insurance Australia Group) and Peter Willcox (AMP and Mayne).

Johnston and Strong and the only two without at least one substantial piece of performance baggage from their careers as professional directors. There is no culture of accountability at the very top of corporate Australia.

Professional directors who overcommit themselves inevitably have disasters on their watch. Notable examples include Stan Wallis, Graham Kraehe, Geoff Tomlinson, Margaret Jackson, John Ralph, Ian Burgess and Dick Warburton.

There is movement in the right direction on this workload front but there are still too many former CEOs dominating the directors' club.

We need more lawyers, accountants, IT and advertising independents who have severed commercial links and can diversify board skill sets.

5. Non-binding votes on executive pay and CEO contracts

This is a powerful tool and worth proceeding with. It has been a success in the UK and there have been no problems with the likes of BHP-Billiton, Brambles and Rio Tinto improving their executive pay disclosure since becoming dual-listed in the UK.

The debate over executive pay has been overdone in Australia and institutions are now routinely voting against CEO options packages, most notably with the rejection of the News Corp proposal last October.

However, we still have 43 executives of Australian companies who received more than $3 million in total benefits in 2002 and 2003. Many were undeserving and we need a system that discourages large payouts to poorly performing CEOs such as George Trumbull, Denis Eck and Keith Lambert. The non-binding votes should do this.

CEO contracts should be released in full as occurs in the US and we should encourage the emerging UK system of rolling one-year CEO contracts as these minimise the golden parachutes.

If executive pay continues to spiral excessively, why not consider a system whereby shareholders must approve the total pay for a company's top 5 executives? This would be no different to the cap on overall annual cash payments to non-executive directors.

6. Disclosure of institutional voting and compulsory voting

The Americans have moved to full public disclosure of institutional voting from January 1 and we should do the same to get some more accountability.

For instance, AMP blew up $10 billion in the UK yet two long serving directors and committee chairs, Richard Grellman and Lord Killearn, were returned with 81 per cent of the vote last year despite terrible performance. Who were the brave souls who voted against them?

Disclosure of voting is particularly important because invisible institutions keep returning dud directors with 99% yes votes and we need to know who is doing this for better institutional accountability. Suggestions of possible blackmail are ridiculous given the pathetic lack of a shareholder pressure in Australia.

Similarly, it is worth considering compulsory voting if we continue to get poor turn outs such as the 30 per cent of AMP shares voted at last year's AGM. The early signs are that electronic voting platforms by custodians are dramatically increasing voting rates so mandating voting will hopefully not be necessary.

7. Related party transactions

All related party transactions must be disclosed. You can't have Rick Allert sitting on the board of Southcorp as chairman and Coles Myer as deputy chairman when the $100 million-plus in dealings between the two companies is not disclosed. Boards argue that being a director is not "a financial interest".

Similarly, some of Solomon Lew's dealings with Coles Myer were also excluded through this technicality. Another example is Southern Cross Broadcasting not disclosing its dealings with the law firm Corrs Chambers Westgarth when its chairman John Dahlsen is a consultant to Corrs and has an office there.

Complete disclosure of director related parties might run to many pages in a major bank annual report but it would also highlight the incestuous nature of the directors' club and the potential conflicts that arise when you have a very concentrated corporate sector, especially in financial services.

8. Definitions of independent directors

The ASX Corporate Governance guidelines make some useful suggestions on this score but the theory will be tested in the upcoming News Corp/Queensland Press deal when three former News Corp executives and some close friends of Rupert Murdoch will sit on the "independent" board committee overseeing arguably the largest related party transaction in Australian corporate history.

Professional non-executive directors need to be completely independent. Consultancies with investment banks and Big Four accounting firms must be thoroughly disclosed and generally discouraged. For instance, Graham Kraehe should not have kept an office with JB Were and Geoff Tomlinson should not have had an office and consultancy with PwC.

9. Disclosure of options and director dealings

We need better disclosure of options for senior management as few companies reveal the terms of earlier option issues when asking for an additional allocation to their CEO. A recent example is Westpac where CEO David Morgan was already about $20 million in front on his existing options but shareholders were not told this as they prepared to vote on another large allocation.

Similarly, companies should provide historical records of option issues and all director shareholdings so shareholders can properly track what their boards are doing.

Directors should also be compelled to disclose all derivative dealings in the company's stock. At the moment people like Macquarie chairman David Clarke and Woolworths CEO Roger Corbett have only disclosed their so-called "cap and collar" options deals voluntarily. Director dealings should also be disclosed on the following day as they can often be price-sensitive

10. Director retirement schemes

Generous lump sum payments based solely on years of service are thankfully being progressively phased out as they act as good behaviour bonds and discourage resignations on matters of principle.

Payments to non-executive directors should be limited to one shareholder resolution covering all payments rather than the current system whereby shareholders approve a maximum annual cash payment and a separate lump sum retirement payout which is often not disclosed properly until after the director has resigned.

The retirement scheme and accrued benefits should be explained in full in every annual report. Just disclosing the annual accrued retirement benefit for that year is not enough as shareholders should be told each year what the trigger points (ie 10 years, 15 years) for increased payouts are when assessing whether to re-elect a director.

Clearly directors should not be able to contract away shareholder approval on retirement schemes as John Ducker did at Aristocrat.

11. ASIC fines

ASIC fines for disclosure breaches should be increased to up to $1 million and directors who fail to reveal their dealings should face forfeiture of the proceeds.

Who can forget the way One.Tel's New York-based director Steven Gilbert sold $90 million worth of shares without telling the market?

12. Mandatory reporting of fraud

With containment of brand damage all the rage these days, there are more and more companies prepared to cover up fraud. The reporting of fraud to authorities should be mandated of directors and company officers.

How did NAB not disclose that an employee had made $10 million punting AMP shares at the time of its $1 billion market raid last year?

Westfield and News Corp are just two companies which have declined to report Victorian executives to police who have been sacked for stealing company funds.

13. Shareholder vote disclosure

Companies should reveal the number of shareholders who vote for and against resolutions as well the total amount of shares voted.

This would make public the substantial number of resolutions each year which are passed by compliant institutional investors when a majority of voting shareholders have actually opposed it.

The best example of this is the BHP-Billiton merger which was substantially opposed by smaller shareholders. Given schemes of arrangement require approval from a majority of shareholders who vote, surely it would make sense to extend disclosure of this across other corporate votes.

14. Audit independence

The proposed changes are worthwhile and it was wise not to adopt the full Sarbanes-Oxley provisions which are arguably excessive, especially for smaller companies.

The worst example we've seen of auditors joining management is Christopher Lewis who went from KPMG's audit signing partner on National Australia Bank to global head of risk management at NAB. Problem was the that he totally missed the Homeside losses in the 2000 accounts head which didn't even mention the MSR risk was at the heart of the $4 billion-plus loss. Lewis was recently fired over the forex scandal.

Given the HIH debacle, a cooling off period of at least two year is certainly appropriate before an auditor should join a board.

Any why shouldn't ASIC appoint auditors? The criteria could them be far more robust and auditors could be fired for being too compliant.

15. ASX structure

The ASX should come under formal price monitoring by the ACCC as it is a government-mandated monopoly providing shareholders with unmatched returns in the Australian market. The regulatory aspects of the ASX should be returned to a not-for-profit structure.

The ASX still can't cope with elementary technical issues such as making historical company announcements available on a name change.

Corporate memory is lost with the withdrawal of historical announcements from failed companies as soon as they stop paying the ASX. Wouldn't it be good to be able to look back at the Pasminco, One-tel and HIH ASX announcements?

16. Audited statements should bear some resemblance to market values

Directors and auditors should be required to explain to shareholders why there is any substantial difference between claimed net assets in a balance sheet and the value reached by the market.

For instance, NAB is currently valued by the market at $47 billion yet it only declares net assets of $25 billion in its balance sheet and is about to announce writedowns as the new CEO clears the decks. Full funding of the NAB's UK pensions schemes should be a mandatory requirement but the balance sheet will be even less accurate after this exercise and the reasons for this should be explained.

A better example is Westfield Holdings which claims it only has net assets of $1.62 billion when the market values the company at $8 billion? The same auditor, Brian Long from Ernst & Young, signed the 2002 AMP accounts claiming it was accurate to claim it had $18 billion in net assets when an accurate picture would have been about $6 billion.

What is the point in mandating auditing if the system allows results which are clearly misleading. On what basis should the News Corp accounts claim a $15 billion asset in BskyB is actually worth zero?

17. Vote counting rules and identification of shareholders

The Corporations Law should specify what information on proxy voting is permitted to flow between a share registry service provider and the board. For instance, as an outside candidate I'm never been provided with any running proxy tallies but the boards sometimes get these. Similarly, there should be provisions guaranteeing access to the share register and to scrutineer voting in contested director elections.

In 18 board tilts I've never been provided with a full list of shareholders when this sort of thing is standard practice in political elections. John Fairfax told me it would cost about $5000.

Only the ASX and AMP have had the courtesy to provide a list of the top 100 beneficial shareholders during a contested election. Given that companies routinely search their beneficial shareholders this should be made public to all shareholders.

Finally, why can't the mandatory top 20 shareholders in an annual report be the beneficial owners rather than various nominee companies?

18. Board nomination rules

The reason I ran for so many boards is that most companies only require one shareholder signature to nominate. I would prefer to simply propose resolutions but getting 100 shareholders to sign for a resolution is too difficult. However, some companies put up nomination barriers by requiring a minimum shareholding (ie AMP and AGL require 2000 shares) or a specified number of shareholder signatures to nominate (Optus 50, Qantas 100, AMP 25).

It would be preferable if this was specified in the Corporations Law but I would be happy if nominating for a board required a small number of signatures such as 6-10.

There is also a major issue over who controls the information sent to shareholders in a contested election. My platforms have been censored by the

likes of Westfield, Commonwealth Bank, NRMA, David Jones, News Corp and Spotless and it really should be an independent body such as the AEC which runs such elections.

19. Proxy voting for board elections

With corporate elections, shareholders should have to tick a box which says "the chairman" if they want to hand over their proxy vote. It is unfair to have this as the default mechanism with reply paid envelopes as it allows a chairman to typically gather up to 10 per cent of the vote.

I was almost elected to the Woolworths board in 2000 but the "open proxies" held by the chairman were enough to get my vote down from 58 per cent to 45 per cent.

Similarly, boards should not be able to unilaterally declare there is no vacancy for an outsider if the total number is within the upper limit specified in the company's constitution. Boards routinely do this meaning that you need to beat an incumbent director to get elected and they typically get 99% of the vote. When you consider the open proxies it is sometimes statistically impossible for an outsider to get elected.

The notice of meeting should declare what the board is doing with open proxies. Aristocrat have failed on this score with John Ducker.

The worst abuse I've seen of this was by Nick Whitlam at the NRMA in 2000 when he used 163 million open proxies against me after the notice of meeting urged shareholders to only tick three of the four boxes because there was no vacancy for the outsider. This reduced my healthy primary vote of 45% (60.5m in favour and 73.2m against) to just 17% after the abuse of inappropriately gathered open proxies.

20. Additional disclosure suggestions

A retailer like David Jones should declare lease liabilities on its balance sheet and also reveal the level of discounts directors are given when they shop at company stores (up to 35%).

Political donations should be disclosed in the annual report to shareholders each year.

Annual board expenses should be revealed to shareholders. For instance, if the board tours Europe, the cost of this should be revealed, just like it is in public sector annual reports. This would also pick up things such as the cost of the two News Corp private jets which are never revealed to shareholders.

If John Howard has to disclose his prime ministerial wine costs, why not the same for public companies with full disclosure of board catering costs.